IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

IN RE: TEL-SAVE SECURITIES LITIGATION	:	MASTER FILE NO. 98-CV-3145
	:	CLASS ACTION
THIS DOCUMENT RELATES TO ALL ACTIONS	:	

M E M O R A N D U M

BUCKWALTER, J. July 19, 2000

Presently before the Court is the Lead Plaintiff's Motion for Class Certification and for Certification as Class Representatives. For the reasons stated more fully below, the Motion is Granted.

I. PROCEDURAL HISTORY

On December 4, 1998 Lead Plaintiffs[1] filed the first consolidated shareholder action, asserting various securities fraud claims against (1) Tel-Save Holdings, Inc. ("Tel-Save" or the "Company"); (2) Daniel Borislow, Chairman of the Board of Directors and Chief Executive Officer of Tel-Save ("Borislow"); and four other officers/directors of Tel-Save (the "Individual Defendants"). The Plaintiffs consist of members of a putative class who purchased Tel-Save common stock and/or related call options, and/or sold related put options in Tel-Save

1. By an Order dated September 15, 1998, this Court appointed the following as Lead Plaintiffs in this matter: Vincent J. Bono ("Bono"); Doron Evans ("Evans"); Layard R. Mace ("Mace"); Raymond Marra ("Marra"); Javanshir Rad ("Rad"); Timothy Stokes ("Stokes") and David Thomas ("Thomas"). Some of the other individuals named Lead Plaintiffs through that Order have since withdrawn.

common stock between August 14, 1997 through May 22, 1998 (the "Class Period"). By an Order dated May 22, 1999, the Court denied Defendants' Motion to Dismiss with regard to Tel-Save, but granted dismissal in favor of Borislow and the Individual Defendants. Plaintiffs filed the Second Consolidated Amended Class Action Complaint ("Second Complaint") on June 18, 1999. The Second Complaint restated allegations against Tel-Save, but named only Borislow as an individual defendant. Borislow filed a Motion to Dismiss which was denied by an Order dated October 19, 1999. Therefore, Borislow and the Company are the remaining Defendants. Now, Lead Plaintiffs seek to be certified as Class Representatives of the following Proposed Class:

> All persons who purchased the common stock and/or related call options and/or sold related put options of Tel-Save Holdings, Inc. from August 14, 1997 through and including May 22, 1998. Excluded from the Class are the Defendants, all officers and directors of Tel-Save or its subsidiaries, members of Defendants' immediate families, any entity in which Defendants have a controlling interest and the legal representatives, heirs, successors or assigns of any such excluded person.

II. FACTUAL BACKGROUND

Tel-Save is a Delaware corporation with its principal executive offices in New Hope, Pennsylvania. It provides long distance telephone services purchased from third-party carriers throughout the United States both to residential and to small and medium-sized commercial customers. Aside from the costs associated with purchasing the long distance services, Tel-Save's primary business costs relate to the marketing of its services and the solicitation of new customers.

Recognizing that the expenses incurred in marketing its telephone services far exceeded its initial revenues, Tel-Save began to out source a majority of its direct telemarketing

services to companies referred to as "partitions." A partition is an independent long distance provider and marketing company that contracts with Tel-Save to purchase and provide long distance services to customers. Partitions generally receive the difference between the amount received from customers and the amount charged by Tel-Save. Tel-Save has stated publicly that it has a policy of promoting increased marketing activities of certain of its partitions by advancing loans to them.

Plaintiffs contend that, as early as August 14, 1997 and continuing throughout the class period, Defendants embarked on a scheme to artificially inflate the price of Tel-Save common stock by concealing and failing to record properly on its statements millions of dollars in marketing costs and other expenses, by disguising the expenses as loans to partitions. As a result, according to Plaintiffs, Defendants misrepresented their marketing expenses, income, results of operations, and overall financial condition.

Specifically, Plaintiffs focus on alleged misrepresentations and omissions made by Defendants related to the loans they advanced to two particular partitions, American Business Alliance ("ABA") and Group Long Distance ("GLD"). Plaintiffs contend that Tel-Save falsely proclaimed that loans made to these entities were adequately collateralized by their assets. Plaintiffs allege, however, that both ABA and GLD were insolvent, that the loans were not fully collectible, and that as a result, Tel-Save was required under the Generally Accepted Accounting Principles ("GAAP") to provide for reserves, including a complete write-off (if appropriate) for the probable losses resulting from such advances and a deduction of these amounts from Tel-Save's reported income. Plaintiffs further maintain that ABA and GLD used the proceeds of the loans to pay Tel-Save's marketing expenses, which otherwise should have been reported as an

expense on Tel-Save's own financial statements. Thus, as a result of Tel-Save's accounting practices, Plaintiffs claim that Tel-Save overstated its income, causing an overpricing of its stock during the class period.

In further support of their claims for securities fraud, Plaintiffs contend that Defendants utilized improper methods of accounting to forgive ABA's and GLD's indebtedness to Tel-Save. As a result, Plaintiffs allege that Tel-Save's financial statements and earning reports for the quarterly periods ending June 30, 1997, September 30, 1997, March 31, 1998, and for the calendar year ending December 31, 1997 were false and misleading. Initially, as to Tel-Save's dealings with ABA, Plaintiffs allege that Tel-Save failed to record accurately the loan forgiveness between the two in December of 1996. Specifically, Plaintiffs claim that Tel-Save misled the investing public by recording the transaction as an acquisition of ABA's assets when, in actuality, Tel-Save forgave approximately $11 million of ABA's indebtedness. Plaintiffs further maintain that Tel-Save acquired ABA with no reasonable expectation of recovering the assets purchased because ABA's total liabilities exceeded its assets by $12 million. By accounting for the acquisition in this manner, Plaintiffs claim that Tel-Save amortized its marketing expenses through the advances made to ABA, rather than immediately expending such costs as they were incurred.

The focus of Plaintiffs' complaint, however, is on Tel-Save's relationship with its primary partition, GLD. Plaintiffs once again allege that, as the uncollectible receivables from GLD accumulated, Defendants improperly eliminated the loan advances from Tel-Save's books without recognizing a loss from forgiveness of indebtedness. Specifically, Plaintiffs contend that Defendants financed GLD's purchase of all of the assets of two unrelated partitions, Great Lakes

Telecommunications, Inc. ("Great Lakes") and Eastern Telecommunications Inc. ("ETI"), both of which possessed conditional warrants to purchase, at significantly below-market prices, Tel-Save common stock. The warrants were allegedly worthless to these unrelated partitions as they were conditioned upon the partitions achieving presumptively unattainable levels of sales of Tel-Save services and required Tel-Save's consent prior to their exercise. At some time later, GLD either sold the warrants directly to Tel-Save at a substantial premium or exercised the warrants themselves, thereafter selling the underlying Tel-Save common stock and giving the proceeds to Tel-Save. As a result, Plaintiffs maintain that GLD was able to retire approximately $20 million of debt owed to Tel-Save without expending any of its own money. Thus, Plaintiffs contend that, through the artifice of acquisitions, Tel-Save was able to convert GLD's uncollectible receivables into cash, ultimately resulting in Tel-Save overstating its income in 1997.

Plaintiffs contend that on May 22, 1998 the improper nature of the relationship between Tel-Save and its partitions was revealed when an on-line financial publication for investors, TheStreet.com, posted a response letter from Defendant Borislow to two minority shareholders of GLD. Previously, on May 7, 1998, the two minority shareholders had written a letter to Defendant Borislow demanding full disclosure of Tel-Save's relationship with GLD, and its use of the warrants held by Great Lakes and ETI to pay off debts owed to it by GLD.

Plaintiffs claim that this disclosure did not immediately affect the price of Tel-Save common stock. However, Plaintiffs contend that, following the release of this letter, the market recognized that Tel-Save's financial statements were not fairly presented and as a result, the price of Tel-Save common stock dropped from its class period high of $30.000 per share to a low of $4.875 per share on October 7, 1998.

Based on these allegations, Plaintiffs assert that each Defendant knowingly and recklessly violated § 10(b) of the Securities Exchange Act of 1934 and Rule 10(b)-5. Plaintiffs further assert that Defendant Borislow is liable under § 20(a) of the Securities Exchange Act as a control person by virtue of his high-level position, his ownership and contractual rights, and his knowledge of Tel-Save's financial condition and operations.

III. LEGAL STANDARD

To obtain certification, Lead Plaintiffs must satisfy the four prerequisites of Fed. R. Civ. P. 23(a), along with a showing that the action is maintainable under one of the subsections of Fed. R. Civ. P. 23(b). See Amchem Prods., Inc. v. Windsor, 117 S. Ct. 2231, 2245 (1997); accord Barnes v. American Tobacco Co., 161 F.3d 127, 140 (3d Cir. 1998) (quoting Amchem). Plaintiff, as the proponent of the putative Class, has the burden of establishing a right to class certification. See Davis v. Romney, 490 F.2d 1360, 1366 (3d Cir. 1974).

In determining the appropriateness of class certification, a court must examine carefully the factual and legal allegations. See Barnes, 161 F.3d at 140 (citing General Tel. Co. of the Southwest v. Falcon, 457 U.S. 147, 160 (1982)). But, the court's findings are not on the merits because, for the purposes of class certification, the court must "refrain from conducting a preliminary inquiry into the merits." Id. (citing Eisen v. Carlisle & Jacquelin, 417 U.S. 156, 177-78 (1974)). Thus, when doubt exists concerning certification of the class, the court should err in favor of allowing the case to proceed as a class action. See Eisenberg v. Gagnon, 766 F.2d 770, 785 (3d Cir.), cert. denied, 474 U.S. 946 (1985).

IV. DISCUSSION

A. Fed. R. Civ. P. 23(a) Prerequisites

Under Rule 23(a), one or more members of a class may sue as representative parties on behalf of the entire class only if (1) the class is so numerous that joinder of all members is impracticable (numerosity); (2) there are questions of law or fact common to the class (commonality); (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class (typicality); and (4) the representative parties will fairly and adequately protect the interests of the class (adequacy of representation). "The requirements of Rule 23(a) are meant to assure both that class action treatment is necessary and efficient and that it is fair to the absentees under the particular circumstances." Baby Neal ex rel. Kanter v. Casey, 43 F.3d 48, 55 (3d Cir. 1994).

1. Rule 23(a)(1) -- Numerosity

To meet the numerosity requirement, "[t]he court must find that the class is 'so numerous that joinder of all members is impracticable.'" In re the Prudential Ins. Co. of Am., 148 F.3d 283, 309 (3d Cir. 1998) (quoting Fed. R. Civ. P. 23(a)(1)), cert. denied, 119 S. Ct. 890 (1999). Impracticability of joinder does not mean impossibility, but rather that the difficulty or inconvenience of joining all members of the putative class calls for class certification. See Pabon v. McIntosh, 546 F. Supp. 1328, 1333 (E.D. Pa. 1982) (Shapiro, J.). Impracticability itself depends on an examination of the specific facts of each case and imposes no absolute numerical limitations. See General Tel. Co. of Northwest, Inc. v. EEOC, 446 U.S. 318, 329 (1980); see also Gurmankin v. Costanzo, 626 F.2d 1132, 1135 (3d Cir. 1980) ("We believe that the numerosity requirement must be evaluated in the context of the particular setting . . ."); Ardrey v.

Federal Kemper Ins. Co., 142 F.R.D. 105, 109 (E.D. Pa. 1992) (Huyett, J.) (stating that the number in the class is not, by itself, determinative). It is sufficient to say that in this case, where the Plaintiffs allege that hundreds of investors have been defrauded, that the numerosity requirement is met.

2. Rule 23(a)(2) -- Commonality

The commonality inquiry asks whether "there are questions of law or fact common to the class." Fed. R. Civ. P. 23(a)(2). This "requirement will be satisfied if the named plaintiffs share at least one question of fact or law with the grievances of the prospective class. Because the requirement may be satisfied by a single common issue, it is easily met. . . . Furthermore, class members can assert such a single common complaint even if they have not all suffered actual injury; demonstrating that all class members are subject to the same harm will suffice." Baby Neal, 43 F.3d at 56 (citations omitted). Accordingly, "'the threshold of commonality is not high.'" In re School Asbestos Litig., 789 F.2d 996, 1010 (3d Cir. 1987) (quoting Jenkins v. Raymark Indus., Inc., 782 F.2d 468, 472 (5th Cir. 1986)), cert. denied, 479 U.S. 852, 915 (1986). Assuredly, "[a] finding of commonality does not require that all class members share identical claims, and indeed 'factual differences among the claims of the putative class members do not defeat certification.'" In re Prudential, 148 F.3d at 310 (quoting Baby Neal, 43 F.3d at 56).

The Lead Plaintiffs claim that the Commonality requirement of Rule 23(a)(2) is met because there are several common questions of law and fact:

(1) Whether the federal securities laws were violated by Defendants' acts alleged in the Complaint;

(2) Whether the statements made by the Defendants misrepresented and/or failed to disclose material facts about the Company's business, operations and financial condition and performance, as more particularly alleged in the Complaint;

(3) Whether Borislow is a "controlling person" of the Company within the meaning of Section 20 of the Exchange Act;

(4) Whether the market price of the Company's Securities was artificially inflated during the Class Period due to the material misrepresentations, deceptions and/or non-disclosures alleged in the Complaint; and

(5) Whether the member of the Class have sustained damages, and if so, the proper measure of such damages.

The Plaintiffs have demonstrated that there are at least several common questions of law or fact that will be important to the case's outcome. Therefore, the Lead Plaintiffs have met the commonality requirement of Fed. R. Civ. P. 23(a).

3. Rule 23(a)(3) -- Typicality

While similar, the typicality requirement is distinct from commonality. "Typicality asks whether the named plaintiffs' claims are typical, in common-sense terms, of the class, thus suggesting that incentives of the plaintiffs are aligned with those of the class." Baby Neal, 43 F.3d at 55. "The typicality criterion is intended to preclude certification of those cases where the legal theories of the named plaintiffs potentially conflict with those of the absentees by requiring that the common claims are comparably central to the claims of the named plaintiffs as to the claims of the absentees." Id. at 57. "[F]actual differences will not render a claim atypical if the claim arises from the same event or practice or course of conduct that gives rise to the claims of the class members and if it is based on the same legal theory." Hoxworth v. Blinder, Robinson & Co., 980 F.2d 912, 923 (3d Cir. 1992). Commonality and typicality overlap in that

they hinge on whether the class members have similar claims. However, commonality tests the sufficiency of the class itself by focusing on the class claims, while typicality tests the sufficiency of the named plaintiff by focusing on the relation between the named plaintiff and the class as a whole. See Hassine v. Jeffes, 846 F.2d 169, 176 n.4 (3d Cir. 1988).

The Lead Plaintiffs in this action allege that their losses occurred due to misleading representations by Tel-Save. Among the Lead Plaintiffs are individuals who traded exclusively in stocks, exclusively in options and those who traded both. Their claims are typical because, even if the specific securities held by other Class members did not change value based on a *particular misrepresentation*, the types of misrepresentations and actions alleged against Tel-Save caused losses for all members of the Proposed Class. The Lead Plaintiffs based their claims on fraud and misrepresentation, the same legal theories as the other Class Members. Therefore, the typicality requirement is satisfied.

4. Rule 23(a)(4) -- Adequacy of Representation

This inquiry requires a finding that "the representative parties will fairly and adequately protect the interests of the class." Fed. R. Civ. P. 23(a)(4). Adequate representation encompasses two distinct inquiries designed to protect the interests of the absentee class members. First it requires that the plaintiff's attorney be qualified, experienced, and generally able to conduct the proposed litigation. Second, it serves to uncover conflicts of interests between named parties and the class they seek to represent. See, In re: Prudential, 148 F.3d at 312; Wetzel v. Liberty Mut. Ins. Co., 508 F.2d 239, 247 (3d Cir.), cert. denied, 421 U.S. 1011 (1975) (Plaintiff's interests must not be antagonistic to members of the proposed class).

There is no dispute that Plaintiffs Counsel are qualified and experienced in this type of litigation. The real dispute is whether the Lead Plaintiffs will adequately protect the interests of the absent Class Members. Defendant argues that common stock holders have interests that diverge from proposed members who held options. But option traders have standing under Rule 10(b) to seek damages for the affirmative misrepresentations that Defendants allegedly made, just as holders of common stock do. See Deutschmann v. Beneficial Corp., 841 F.2d 502, 506-507 (3d Cir. 1988). Both option and stock holders have an interest in proving that stock prices were artificially inflated by defendants' material misrepresentations and omissions. As mentioned above, Lead Plaintiffs are individuals who traded in both stock and options. Therefore, the Court finds that the Lead Plaintiffs are adequate representatives of the Class at this stage of the proceedings.

B. The Requirements of Rule 23(b)

In addition to the meeting the requirements of Rule 23(a), the Lead Plaintiffs are also required to satisfy the Rule 23(b)(3).[2] Although efficiency requires that common issues predominate over issues that are particular to each class representative, it does not require that there be an absence of any individual issues. See Smith v. Dominion Bridge Corp., 1998 WL 98998 at *5. (E.D. Pa. 1998) (J. Reed). In determining whether common questions predominate, the court's inquiry is directed towards issues of liability. See In re Cephalon Securities Litigation,

2. This section states that a class action is maintainable if the prerequisites of subdivision (a) are satisfied and, in addition, "the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (D) the difficulties likely to be encountered in the management of a class action.

1998 WL 470160 (E.D. Pa. 1998) (J. Green). The main issue in establishing liability in this case will be whether Defendants made misrepresentations which had the effect of artificially inflating the price of Tel-Save securities. The Defendants are correct that there will be different measures of reliance and damages for the common stock holders as compared to option traders. Differences in reliance and damages are typical in securities litigation, and should not be used as bases for denying class certification. See Eisenberg v. Gagnon, 766 F.2d 770, 787 (3d. Cir. 1985) (abuse of discretion for district court to deny certification based on the existence of individual issues as to reliance); Blackie v. Barrack, 524 F.2d 891, 905 (9th Cir. 1975) (individual questions concerning the amounts of damages and reliance are not impediments to class action treatment).

A class action would also be superior to other available methods for the fair and efficient adjudication of this controversy. Separate lawsuits by all potentially affected securities holders would be prohibitively expensive for most plaintiffs and an inefficient use of judicial resources. Class actions are a particularly appropriate and desirable means to resolve claims based on the securities laws. See Eisenberg, 766 F.2d at 785.

V. CONCLUSION

The Court finds that Lead Plaintiffs and Counsel will adequately represent the Proposed Class on the central issue of this case: whether Defendants made material misrepresentations that artificially inflated the price of Tel-Save stock. The Court also finds that a Class Action would be a superior means of adjudicating this controversy. Therefore, the Court will certify the Proposed Class and certify the Lead Plaintiffs as Class Representatives.

An appropriate order follows.

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O R D E R

AND NOW, this 19th day of July, 2000 upon consideration of the Plaintiffs' Motion for Class Certification (Docket No. 35), the Defendants' response thereto (Docket No. 52), and the Plaintiffs' Reply (Docket No. 60); it is hereby **ORDERED** that the Motion is **GRANTED.**

The Lead Plaintiffs are CERTIFIED as Class Representatives of the following certified Class:

> All persons who purchased the common stock and/or related call options and/or sold related put options of Tel-Save Holdings, Inc. from August 14, 1997 through and including May 22, 1998. Excluded from the Class are the Defendants, all officers and directors of Tel-Save or its subsidiaries, members of Defendants' immediate families, any entity in which Defendants have a controlling interest and the legal representatives, heirs, successors or assigns of any such excluded person.

BY THE COURT:

RONALD L. BUCKWALTER, J.